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SUBJECT: NIGERIA: NATIONAL TAX POLICY ELICITS MIXED RESPONSES

¶1. (SBU) Summary: Nigeria's Draft National Tax Policy (DNTP) proposes sweeping reforms to the current tax system, including a shift from direct to indirect taxation; a simplified tax regime; and centralized tax authorities at the federal level. The private sector considers the formulation of a national tax policy a positive development in the Federal Government's effort to improve business environment while Lagos State fears it will hurt state coffers and undermine the formal market economy. End Summary.

More Indirect Taxation, Centralized Tax Authority

¶2. (U) The Presidential Committee on Tax Policy recently released its Draft National Tax Policy (DNTP). The Committee, which included the Minister of Finance and the head of the Federal Inland Revenue Service, proposed a shift in focus from direct taxation to indirect taxation by lowering the corporate tax rate from 30 to 20 percent and lowering the personal income tax rate from 25 to 17 percent and gradually increasing the value added tax (VAT) rate from 5 to 15 percent by 2009. The DNTP also recommends centralizing tax authority at the federal level to reduce multiple taxations and to improve tax administration. The Ministry of Finance would have more tax oversight and coordinate tax policy. The National Assembly will have the power to change tax rates, and a Joint Tax Board (comprising of federal and states tax agencies) will administer personal income tax across the states. The Committee recommended the eventual inclusion of the National Tax Policy (NTP) in the constitution as well as its comprehensive review every three years.

DNTP Contains "Oddities"

¶3. (SBU) Russel Eastaugh, Director Tax Services, PriceWaterhouseCoopers Ltd., told EconOff on August 14 that the DNTP contains a plethora of tax "oddities", including a two percent levy on corporate profits for a "Police Fund", which Eastaugh says will add to the effective costs of doing business in Nigeria and could undermine the DNTP's overriding objective of reducing multiple taxation to encourage investment. In Eastaugh's view the corporate income tax also contains opaque incentives like the "pioneer industry tax exemption" which gives a tax holiday of up to five years to companies deemed "vital to Nigeria's national interests". According to Eastaugh, although consultant firm KPMG and the International Monetary Fund (IMF) informally provided inputs

throughout the drafting process, the Committee did not formally engage the services of tax experts.

VAT Increases to Hurt Lagos State Formal Economy

¶4. (SBU) Eastaugh said the proposed VAT increases would end up hurting commercially advanced states like Lagos. Ade Ipaye, Lagos State Special Adviser on Taxation and Revenue, told EconOff August 21 that the additional gain from VAT would not be commensurate with the revenue lost from income tax reduction. (Lagos State keeps 100 percent of the personal income tax collected in the state.) Lagos State Government (LASG) is challenging in the Supreme Court the Federal Government's (FG) power to administer a VAT in all 36 states.

¶5. (SBU) Because VAT effectively constitutes a consumption tax in Nigeria, VAT increases would hurt manufacturers, retailers, and consumers operating in the formal economy, Ipaye said, fearing that retailers and consumers would shift to the informal economy to avoid paying the VAT. Jide Mike, Director General of the Manufacturing Association of Nigeria, told EconOff August 15 that the proposed VAT would only add to already soaring business costs.

New Tax Policy Will Improve Business Environment

¶6. (U) Eastaugh said a National Tax Policy, with the right formulation and administration, would improve Nigeria's business environment. Although the DNTP contains some weaknesses, the concept of a simplified and centralized tax framework was a good starting point. The Committee's effort to solicit stakeholder

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inputs was laudable, he said. Linking sensible tax policies with administrative efficiencies will be a challenge as will changing the mindset that non-oil taxes do not play an important role in the FG's revenue base.

¶7. (SBU) Comment: A national tax policy, properly crafted, professionally administered and equitably enforced, would undoubtedly help improve the business environment. Those are big challenges since Nigerian politicians and bureaucrats are accustomed to an ineffective tax system propped up by proceeds from the oil industry. This tax plan appears to be a step in the right direction. End Comment.

Blair